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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1940

No. 253

EUGENE HIGGINS,

Petitioner,

vs.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

SELDEN BACON,
Counsel for Petitioner.

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Eugene Higgins prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Second Circuit, entered May 22nd, 1940, in the above entitled cause, affirming two orders of the United States Board of Tax Appeals.

Opinions Below.

The opinion of the Circuit Court of Appeals (R. 243) is reported in 111 F. (2d) 795. The opinion of the Board of Tax Appeals (R. 68-86) is reported in 39 B. T. A. 1005.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered on May 22nd, 1940 (R. 245).

The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

Questions Presented.

The following questions are presented:

1. Where an individual, having large investments in both income-producing real estate and in securities, devotes his personal time and attention to the management, care and supervision of both types of investments, and necessarily maintains offices and employs salaried clerks to assist him in the activities incident thereto as a single and entire enterprise, does the Revenue Act of 1932 make a distinction between the general management expenses which, though undivided in themselves, were deemed attributable to the management of the real estate (which concededly are deductible as business expenses), and those deemed attributable to the management of the securities, and authorize the Commissioner to apportion the expenses of the undivided management and disallow any deduction for those he deems attributable to the management of the securities?

2. Cannot the management of investments in securities by the owner, when, in addition to his own personal constant supervision and control, the services and time of several employees is needed to carry on that management, be a "business" within the meaning of Section 23 (a) of the Revenue Act?

3. Does the Revenue Act make a distinction between the ordinary and necessary expenses of managing investments

in securities as a business, and those of managing investments in real estate as a business?

4. Where the management of investments in securities amounting to many millions of dollars would be business if conducted for hire by a third person for the owner, does the conduct of the same affairs cease to be "any * * * business" solely because conducted by the owner himself with the assistance of a staff of salaried employees?

Statute Involved.

The only statute applicable to the issues involved is Section 23 (a) of the Revenue Act of 1932, which reads as follows:

"SEC. 23. DEDUCTIONS FROM GROSS INCOME.

"In computing net income there shall be allowed as deductions:

"(a) EXPENSES.—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; and rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity."

Statement of Facts

Petitioner is an American citizen, possessed of investments in real estate having an assessed value of over $11,000,000 (R. 135-145) and in securities consisting of stocks and bonds of an estimated value of over $25,000,000 (R.

125). For the purpose of managing these investments, petitioner more than forty years ago (R. 119, 128) set up a substantial business organization, which it costs him approximately $75,000 a year to operate (R. 50-51, 52-54). All of the petitioner's real estate, with the exception of two small unimproved plots, is located in the Borough of Manhattan, New York City, and consists of thirty different plots on which the improvements alone are assessed at $3,466,000 (R. 118, 135-145). His securities are kept in safe deposit boxes in New York City (R. 121-122). Petitioner has for many years resided at Paris, France, where he personally conducted his affairs and directed all details of the operation of his organization (R. 119-120, 125-126, 129, 148-199).

All details of petitioner's financial affairs are conducted through his New York office pursuant to his personal detailed instructions. His income consists of rents, dividends and interest, all paid to him at his New York office (R. 123).

In Paris, he has an office in a building separate from his dwelling consisting of several rooms equipped with cabinets, desks, typewriters and a library in charge of his private secretary (R. 114, 120, 127). Duplicate sets of his New York books of account are kept there (R. 128, 129).

In New York City he rents a suite of four offices staffed with a manager, a real estate man, an accountant, one consultant, and a clerk-stenographer (R. 114). This entire staff of the petitioner consists of salaried employees whose time (with the exception of that of one employee whose activities were confined to the real estate), was indiscriminately given to management of real estate and management of investments in securities.

The evidence to the personal management and control and personal direction by the petitioner of these investments is full and uncontradicted.

That the expenses which he claimed as a deduction from his gross income were usual, ordinary and necessary was undisputed.

That, so far as concerned his holdings of real estate, he was conducting a business within the meaning of the Act was conceded and held below (R. 79).

But the Board of Tax Appeals and the Circuit Court of Appeals supported the Commissioner in drawing a hitherto unknown distinction between the expenses of management of real estate and those of management of investments in securities and allowed a percentage of about two-thirds of his annual expenses as attributable to the management of his real estate, and decided that about one-third of his expenses in each year must be attributed to the cost of management of his securities; and that for so much of the expenses of the business so conducted by him as pertained to the investments in securities he should not be allowed a deduction; and this although the entire management under him was conducted in common by a single staff of salaried employees. The apportionment of the expenses (excepting the salary of a single employee whose time was practically entirely devoted to the real estate), was not based upon any positive evidence, but was estimated by the Board of Tax Appeals on the basis of the time supposed to be given to the one or the other. There is no pretense that there was any such actual division in the expenses as incurred.

No question has been raised as to the correctness of the apportionment so made, but that it was essentially a guess is apparent on every page of the record. No such actual division of the expenses for carrying on the business by salaried employees was or could reliably be made in the office operations.

Without burdening the court at this time with any detailed statement of this evidence, we may refer the court to the following pages of the record: 114-121, 123, 124,

127-130, 134, and 148-199, where all this is gone into in detail (See also pages 68-79).

The case presented is not one of letting others run his affairs, simply sitting back and merely receiving income from a capital managed by others. It is one of direct personal management of all his affairs giving daily attention to all its details, which are all controlled by him personally, though, owing to the magnitude and multiplicity of these affairs, he requires the services of salaried assistants subject to his orders.

That, in this case, attending to investments in securities amounting to upwards of twenty-five million dollars attained the dimensions of a business operation, is clearly established by the determination that the share of the ordinary and necessary annual office rents, expenses and salaries of employees held applicable to the management of these investments in securities (for which portion of the rents, expenses and salaries paid by him deduction is denied) amounted in one of the years under consideration to over $20,000 and in the other to over $17,000 (R. 50-54, 85-86, 87, 88).

It is conceded and found that he was engaged in business. It is also conceded and found that the expenses for which he claimed the rejected deduction were ordinary and necessary expenses paid by him.

The Commissioner and the court below have, however, taken the position that, while his management and care of his real estate was business, the management and care of his securities, though attaining such magnitude, was not "business"; and they accordingly have divided the expenses of operating his offices, consisting of salaries, rentals and miscellaneous general expenses, attributing just over two-thirds of these disbursements to the management of the real estate and the balance, substantially one-third, to the management of the investments in securities, allowing

the two-thirds as a proper deduction but refusing to allow as a deduction the one-third (substantially) of these same expenses, which the Commissioner and the court have deemed to be attributable to the management of his investments in securities.

Specification of Errors to be Urged.

The Circuit Court of Appeals erred:

1. In disallowing the claim of petitioner for deduction from his gross income of the ordinary and necessary expenses paid by him in connection with his personal management of his holdings of securities and new investments therein (R. 244, 245).

2. In holding that petitioner in his personal management of his various investments in real estate and in securities was not carrying on a business and entitled to deduct from his gross income all the ordinary and necessary expenses thereof (R. 243-245).

3. In holding that where the petitioner personally managed his entire estate, consisting partly of real estate and partly of investments in securities, all as a single unit, through regular offices maintained by him, and with the aid of a staff of salaried employees, the Revenue Law authorized a segregation of the actual ordinary and necessary expenses of his conduct of those affairs, between those deemed incurred in the management of his real estate and those deemed incurred in the management of his investments in securities, allowing the former as paid in carrying on business, and disallowing the latter as a deduction as not having been paid in carrying on business (R. 244-245).

4. In holding that the ordinary and necessary expenses paid by the petitioner in his personal care and management of his investments in securities, under the undis-

puted circumstances shown by the record, were not expenses of a business carried on by him (R. 244, 245).

5. In holding that "By the common speech of men, a person who does nothing beyond looking after his own investments and receiving the income from them is not conducting a trade or business. He is generally spoken of as 'retired' or 'not in business.' It is forcing the ordinary meaning of words to say that conserving or enhancing one's estate is carrying on a trade or business" (R. 244).

6. In holding that "the attention which the petitioner gave to his investments in stocks and bonds did not amount to carrying on a trade or business, and that expenses paid in caring for such investments were not deductible from gross income" (R. 244).

7. In affirming the decisions of the Board of Tax Appeals disallowing in each year the deduction of such part of petitioner's expenses of his business as it had held to be applicable to the management of his investments in securities (R. 244-45).

Reasons for Granting the Writ.

The decision of the court below is in direct conflict with decisions of other Circuit Courts of Appeal. This is expressly recognized in the opinion of the Circuit Court of Appeals herein from which we quote:

> "The result we have reached is not to be reconciled with Kales *v.* Commissioner, 101 F. (2d), 35, in the Sixth Circuit."

In *Kales* v. *Commissioner*, 101 F. (2d) 35, decided by the Circuit Court of Appeals for the Sixth Circuit on January 12, 1939, the taxpayer was a woman possessed of large holdings in securities and real estate, which she personally

managed. Basing its opinion solely upon taxpayer's personal management of her properties, the court decided that she was in doing so carrying on business, and entitled to have her expenses in connection with the management of all her properties, whether real or personal, deducted from her gross income, as business expenses under Section 23 (a) of the Revenue Act.

In *du Pont* v. *Deputy*, 103 F. (2d) 257, decided by the Circuit Court of Appeals for the Third Circuit on March 28, 1939, Mr. du Pont had two offices with seven or eight employees, the expenses of maintaining which were over $36,000. He had large holdings in securities to the management of which he devoted 50% more or less of his time. Question was raised whether certain expenses of the taxpayer were ordinary and necessary expenses paid by him in carrying on his business. They had been held by the Circuit Court of Appeals to be such, and were allowed by it as a deduction from taxpayer's gross income.

The case then came to this Court. Its decision is reported in 308 U. S. 488; 60 S. C. 363, 84 L. Ed. 313. In this Court three opinions were written.

The prevailing opinion, by Justice Douglas, held that the particular expenses in question were not ordinary and necessary expenses, and took the position that it was consequently unnecessary to determine whether Mr. du Pont in the management of his securities was carrying on business.

Justice Frankfurter wrote a short concurring opinion, joined in by Justice Reed, taking the position that the case ought to be disposed of on the ground that Mr. du Pont was not carrying on business, and that the decision below ought to be reversed on that ground.

Justice Roberts wrote a dissenting opinion, joined in by Justice McReynolds, supporting the position taken by

Judge Maris in the court below that Mr. du Pont was engaged in business.

The question whether the personal management of a vast fund of securities was doing business was thus left open by this Court in the *du Pont* case (four justices expressing divergent opinions concerning that question, and the majority of the Court ruling that the question was not really presented). In the case at bar the question, thus left open in the *du Pont* case, is squarely brought up.

The matter involves determination of the meeting of the words "any * * * business" in the Act. Two Circuit Courts of Appeal, those for the Third and Sixth Circuits, have held that the personal management by the taxpayer of his investments in securities, involving large expense, is carrying on a "business." In the case at bar the Circuit Court of Appeals for the Second Circuit has held that it is not a "business" within the meaning of the Act, though carried on as part of the management of his entire estate, much of which was real estate, and its management concededly a business in which the petitioner was engaged.

It should not pass unnoticed that Congress in enacting the Revenue Act said "any trade or business," evidently giving to the word "business" a wider meaning than was involved in the word "trade." And it is *any* business.

Is it not reasonably to be urged, that Congress in so adding the words "or business," preceded as it was by the word "any," used the word "business" with a meaning as wide as that which this Court had but a couple of years before attributed to that word in construing its use in the provisions of the Tariff Act of 1909 imposing an income tax on corporations?

Flint v. *Stone Tracy Co.*, 220 U. S. 107, 169-171.

The decision of the Circuit Court of Appeals for the Second Circuit in the case at bar is statedly on its face irreconcilable with the decision of the Circuit Court of Appeals for the Sixth Circuit in the *Kales* case. It is also in conflict with the ruling of the Circuit Court of Appeals for the Third Circuit in the *du Pont* case, which this Court found it unnecessary to pass upon.

The decision at bar is also in conflict with the long continued practice of the Bureau of Internal Revenue, of allowing the deduction of the expenses of management of investments in securities as business expenses.

O. D. 537, 2 C. B. 175 (1920);
O. D. 877, 4 C. B. 123 (1921);
I. T. 2579, X-2 C. B. 129 (1931);
I. T. 2751, XIII-1 C. B. 43 (1934);
1934 C. C. H. Fed. Tax Service, Vol. 3, Par 6035.

To these rulings of the Bureau might well be added the further unreported precedents that for the years from 1913 to 1931 no objection was raised by the Commissioner to the allowance as a deduction to this particular taxpayer of all the expenses of his personal management of his estate, without distinction between his investments in real estate and his investments in securities; and in the Commissioner's 60-day letter concerning the 1932 tax he sought only to disallow expenses proportionate to the income from tax-exempt securities (R. 21 and 112). And it was only at the trial before the Board of Tax Appeals that this theory was abandoned and the theory advanced that the deduction should be limited to those pertaining to real estate (R. 110-112).

The question presented has never been passed on by this Court and the situation is not only one of legal construction of the Act on a point where the Circuit Courts of Appeal differ in opinion, but also one frequently pre-

sented. And the question is squarely presented by the record in this case.

Conclusion.

It is respectfully submitted that this petition for a writ of certiorari should be granted and the question set at rest by this Court.

Respectfully submitted,

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